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MetLife®

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STATE OF VERMONT
DEPT. OF INSURANCE

VIA FACSIMILE and FEDERAL EXPRESS

July 28, 2003

Ms. Rebecca C. Heintz
Vermont Division of Insurance
Department of Banking, Insurance
Securities and Health Care Administration
89 Main St., Drawer 20
Montpelier, VT 05620-3101

Re: Market Conduct Exam - MetLife

Dear Ms. Heintz:

Attached is MetLife's response to the Insurance Division's Report of Examination on the Market Conduct Affairs of the Metropolitan Life Insurance Company, Metropolitan Insurance and Annuity Company, Metropolitan Tower Life Insurance Company, and Security First Life Insurance Company.

Please feel free to contact me if you have any questions about the Company's response.

Very truly yours,

Robert F. DiLorenzo

MetLife Response to the
Vermont Market Conduct Report of Examination

MetLife responds as follows to the Report of Examination on the Market Conduct Affairs of the Metropolitan Life Insurance Company, Metropolitan Insurance and Annuity Company, Metropolitan Tower Life Insurance Company, and Security First Life Insurance Company (the "Company").

MULTIDISTRICT LITIGATION (Report pps. 7-8.)

The facts of the multidistrict litigation and related regulatory action settlement (MDL) were provided to Commissioner Elizabeth R. Costle by MetLife Senior Executive Vice-President and General Counsel Gary A. Beller on August 18, 1999. A copy of Mr. Beller's letter and Summary of MetLife's Proposed Settlement Terms were attached to the Company's response of January 30, 2003 as Exhibit 1.

Commissioner Costle was provided details of the settlement and advised at that time that MetLife would be pleased to respond to any questions or requests for additional information. As no inquiry was received from Commissioner Costle, we believed that the Department of Banking, Insurance and Securities ("Department") was satisfied with the terms of the settlement. Further, as noted in the Report, all claims of Vermont Class Members have been resolved in accordance with the approved settlement. Accordingly, with no new facts or issues raised in the Report, MetLife believes the MDL to be a matter previously reviewed and closed by the Department and respectfully requests that the matter not be included in the Report.

FINES, PENALTIES & FORFEITURES (Report pg. 9.)

Vermont Bulletin 30

The Report alleges that the Company failed to file a listing of reportable administrative actions between the insurer and state insurance departments for each of the years 1998, 1999 and 2000 as required by Vermont Bulletin 30. However, the Report then refers to a matter involving a settlement agreement between the United States Government and the Company. The Company believes that such a matter, not involving a state insurance department, need not be included in the report required by Bulletin 30 and requests that the reference be deleted from the Report.

Settlement Agreements

The Report refers to settlement agreements between the Company and the U.S. Government, and the Company and the state of Florida. In addition to the foregoing, the Company entered into a Stipulation with the State of Vermont Department of Insurance ("Stipulation"), by Deputy Commissioner of Insurance Shawn W. Bryan, on July 29, 1994, and based on the Stipulation, and agreed to an Order of the Department of Insurance, by Commissioner Elizabeth R. Costle, on August 11, 1994. Copies of the Stipulation and Order were attached to the Company's response of January 30, 2003 as Exhibit 2.

These matters, particularly those involving the Florida Department of Insurance, have been reviewed by the Department, memorialized through the Stipulation and resolved by the Order of August 11, 1994. The Report does not present any material new facts or reason to reintroduce matters occurring long prior to this Examination period and long resolved in Vermont and other states. Therefore, the Company respectfully requests that this section of the Report be revised to eliminate references to settled matters involving alleged improper sales practices.

SALES AND MARKETING (Report pps 10-11.)

Target Premium Issue

The Report states that "the Company utilizes a 'target' premium as a device to assist prospective purchasers in determining how much premium they may need to pay for a specified amount of insurance". The Report ostensibly defines "target premium" as the minimum amount of premium which the insured would have to pay in order to maintain a specified amount of insurance in force until the scheduled policy maturity date, assuming that the interest rate being credited by the Company to the accumulation value and the policy expenses remain unchanged throughout the life of the policy. The Report further states that "the 'target' premium is of the utmost importance since it is the only figure available to a prospective applicant for use in comparing the cost of the Company's universal life policies with policies of other companies."

The Company disputes the examiners findings, in particular the proffered definition of "target" premium. The Report, in referring to the "Company", gives the false impression that the examiners definition of "target" premium is attributable to MetLife or otherwise taken from Company materials. That is not the case.

The "target" premium is the minimum premium the Company will permit to be shown on the specifications page for issuance of the policy. The amount is not intended as a device for comparison with other companies' products and is not, as alleged, the only figure available to compare similar policies.

The policy is sold with an illustration and is issued with a policy summary. Both of these documents show policy values based on both guaranteed interest rates and charges and current interest rates and charges. These values are the bases used in the industry and with clients for comparing similar products offered by other companies. Cash value at retirement age and minimum premium needed to carry coverage to maturity are very important figures for comparisons which can be determined from the illustration. Only for term policies is premium alone properly used for comparisons. Similarly, current interest rates are not a valid basis for comparison without knowing the level of policy charges and the combined impact on the policy's accumulation fund.

Once the policy is in force, the annual report provided to policyholders shows how long the policy would stay in force based on four scenarios: payment of no further premiums or payment of the planned premium, both at current rates and guaranteed rates of charges and interest credits. This enables the policyholder to understand more about the dynamics of the policy; that is, values are based on premium flow, interest rates and the level of policy charges.

A look at the specifications page of the policy form demonstrates the fact that the target premium is not a key figure. As a matter of fact, the word "target" never appears on the page. The number shown is a **"Planned Premium"** which is the amount of premium the applicant indicates he/she intends to pay into the policy. During the first two years of issue, Company rules require that the Planned Premium be no less than the Target Premium unless an additional lump sum premium is anticipated. The specifications page contains a clear statement that ***"the planned premium shown below may need to be increased to keep the policy and coverage in force"***. There is no guarantee of coverage for the payment of this premium and that fact is made clear to the applicant.

Pursuant to the Vermont Life Insurance Illustrations Regulation (R.I.-98-1) this policy is sold with an illustration which is signed by the applicant. The illustration shows how long the planned premium would keep the policy in force based on guaranteed and illustrative rates. If in fact the premium is not sufficient to carry the policy until age 95, the illustration will show that the accumulation fund, cash value and death benefit will be zero. The summary page of the illustration (which is the page the applicant signs) expressly includes the year of lapse based on guaranteed and illustrative rates. The illustration, if not provided at or before the time the application is taken, is provided at delivery of the policy.

Some of our customers have found universal life policies to be appropriate to provide "temporary" coverage for a longer period than term insurance and at a lower cost than whole life insurance. For these customers, the "target" premium is not the issue; they look to the illustration to determine how long coverage might last under different payment scenarios if rates and charges didn't change. The target premium by itself is not an important number.

An illustration provided to an applicant for insurance on 11/04/97 was provided with the Company's response of January 30, 2003 as Exhibit 3. As indicated on page four of the illustration:

> If the interest rate shown decreases and/or current insurance rates increase, the planned premium outlay may need to be increased and/or continued beyond the number of years shown in order to keep this policy in force and attain the non-guaranteed values and benefits shown in this illustration.

This illustration clearly indicates, based on the planned premium outlay and rates and charges at the time, that coverage would only remain in force to age 83. This illustration was signed by the applicant upon receipt.

No where in the illustration is there any indication that the planned premium (or any "target" premium) would continue the policy to age 95. This applicant opted to pay the minimum planned premium to continue insurance coverage to age 83, based on rates and charges in November 1997.

The Company reminds the Department that universal life insurance policies have at times offered lower cost coverage than term plans. Many prospective term applicants are known to have purchased universal life insurance policies as a less costly limited period alternative to term insurance.

The Report raises an issue with respect to "target" premium and corrective action taken by MetLife (p. 10, par. 4). That matter was a unique situation involving policies issued to residents of Texas and New York. As a result of inquiries made by the insurance departments of those states during the policy filing and approval process, and a drafting error with the policy filings, certain universal life policies issued in those states expressly state that the planned premium would carry the policy to maturity based on current interest rates and current charges. MetLife has made adjustments with respect to those policies in order to honor the language of the policy form. In all other cases, no representation is made with respect to the adequacy of or derivation of the planned premium. In all cases the duration of coverage will be as long as the accumulation fund is sufficient to cover policy charges as stated in the policy.

The Report contains an alleged example of a "target" premium issue (p. 10, par. 3) that is not an actual policy transaction and is otherwise not based in fact with respect to Vermont issued policies. Based on misunderstanding and a created scenario, the Report then makes a recommendation concerning "target" premiums that is wholly unsupported, unwarranted and inappropriate (p. 11, par. 1).

The "target" premium facts are as described above by the Company and not as envisioned by the examiner and reported as fact in the Report. Therefore, the Company respectfully requests the Department remove the "target" premium issue section (pps. 10-11) from the Report.

SUITABILITY (Report pps. 12-19)

The examiners indicated that three annuity cases outlined in the report appear to have been written without reasonable grounds for suitability. (Case I p. 12, Case II pps. 12-13, Case III p. 13.). The Company requests the Department consider all of the following in response.

Written Standards of Suitability (pps. 13-14)

The Report acknowledges the Company's "Manager's Guide to Appropriateness of Sale" ("Guide") and the information provided therein to assist managers in assessing the appropriateness of a sale of an equity product. One of the guidelines noted is with respect to the age of the customer.

The examiners' questioned whether the sales manager applied written guidelines in the Guide and concluded that Cases I, II, and III appear to represent violations of 8 V.S.A. §4724(16). The explanation in the Report appears to indicate that the examiners' concerns and conclusions were based on the age of the owners in the three cases.

The Company understands the Department's concerns about suitability and sales to seniors; but denies that any violation of Vermont law occurred in these cases. The Company requests the Department note the following provisions of the Preference Plus Account (PPA) variable annuity sold to these owners.

The PPA has several features that make it appropriate for clients of any age. Unlike most variable annuities, the PPA has a Fixed Interest Account (two of the three contracts had 100% allocated to this account and the third had over half of her assets allocated to it) rather than a money market account as one of its investment options. The Fixed Interest account provides one-year interest rates and a guarantee that the rate can never be less than 3%. In addition, if 100% of an owner's money remains in the Fixed Interest Account he/she will always get back at least what was remitted to the contract and early withdrawal charges cannot invade the principal. Additionally, and of great importance, is the death benefit protection for the beneficiaries of the PPA. MetLife guarantees that the death benefit will never be lower than the contributions made to an account (minus any withdrawals) even if the account balance has declined because of market fluctuations. This allows an owner to invest in the market and at the same time have assurance that his/her heirs will receive at least the principal. Finally the PPA provides a systematic withdrawal program that allows the owner to withdraw up to 10% of the account balance each year in monthly, quarterly, semi-annual or annual payments without a withdrawal charge. This permits convenient easy access to his/her funds.

The examiners expressed suitability concerns in the three cases based on the clients' ages. However, based on the provisions of the PPA, age alone was not a determinative suitability factor. The Company believes the three referenced cases were suitable sales.

<u>Suitability of Annuity Purchases</u> (pps. 14-19)

The Report acknowledges that the examiners developed a suitability test involving numerical weights assigned to risk categories by the examiners in order to assess fund allocation. Currently, there is no such suitability test from either the SEC, NASD, NAIC or the State of Vermont for determining appropriate fund allocation for the various investment objectives a client can elect.

For a variable annuity with more than 30 funds and a fixed interest account, a given investment objective can be met in multiple ways. Therefore, the Company's position is that any regulatory guidelines to be developed should be qualitative rather than quantitative in nature. Qualitative guidelines would provide discretion to the Contractowner in selecting funds. In addition, a formula approach such as the one used by the examiners can produce results that are unexpected - e.g. investing 50% in Preservation of Capital and 50% in Aggressive Growth would be consistent with an investment objective of Growth and Income. Consequently, even with an objective approach, a further subjective review is required.

The examiners have provided neither facts nor a necessary or appropriate basis to develop such a test. Indeed, the Department has explicitly acknowledged the lack of such a "bright line test for determining suitability" through Insurance Bulletin 129. The Company expects that the Department will recognize, as have other regulatory bodies, that a numerical weight test does not establish a factual basis for determining suitability. Accordingly, the Company respectfully requests that the Department delete the arbitrary weight test, accompanying charts and recommendations based on such testing from the Report.

The Company assures the Department that MetLife's suitability practices are based on our understanding of and experience with selling variable annuities, and are consistent with the recommendations of Insurance Bulletin 129 that factors to be considered in recommending a variable product include the customer's age, tax status, financial objectives, need for immediate liquidity or retirement income, and investment sophistication .

The Report notes that 44 out of 51 cases (p. 17, par. 2) and 39 out of 60 cases (p. 18, par.1) did not contain the Suitability Worksheet and/or Asset Allocation Questionnaire. Please be advised that the Worksheet is not required for issue. The application itself indicates the owner's investment objective, risk tolerance and allocation of funds. If this information does not agree with our guidelines for issuance, further clarification is obtained from the owner over a recorded telephone line. The only time an Asset Allocation Questionnaire is required, is when it is indicated that the sale was made on the basis of the information the owner provided in the Questionnaire.

The Report includes the examiners' recommendation that the Company change the PPA application to include a question as to whether or not a penalty charge will be incurred by the annuitant. The Company does not believe a change in the application is necessary as the Company requires, in addition to the Vermont state replacement form, completion of an Annuity Replacement Questionnaire that includes the following question about the transaction: Will there be a surrender charge on your existing policy/contract as a result of this transaction? Yes/No. If "Yes", indicate the approximate dollar amount. A copy of the MetLife Annuity Replacement Questionnaire is attached as Exhibit 1. The Company respectfully requests the examiners' recommendation be deleted from the Report.

POLICY FORM FILINGS (Report p. 21)

The Report indicates that Long Term Care contract #81207-0010 contained an enrollment form identified as EF. 1096-5 for which the Company failed to obtain filing and approval from the Department. The Company has not been able to locate the form as identified and respectfully requests the Department provide a copy for review.

CLAIMS PROCEDURES AND PROCESSING (Report pps. 22-23)

As noted in the Report, the Company agreed to re-calculate the interest rate on certain paid life insurance claims and send additional payments to claimants where necessary. The Company has completed the process of making those payments to claimants.

POLICY LOAN INTEREST (Report p. 24)

The report asserts that the Company charges a rate in excess of 8% on policy loans in violation of 8 V.S.A. Section 3731.

The Company denies that it charges a rate in excess of 8% on policy loans.

This policy form was filed with and approved by the Vermont Insurance Department. The policy form clearly states that policy "loan interest is charged daily at the rate of 8% a year" and that "a loan may affect the interest rate we credit" to the accumulation fund. The 8% rate is clearly in accord with 8 V.S.A. 3731.

The policy further states that:

> If there is a loan against this policy, interest on that portion of the accumulation fund in excess of $1,000 that equals the loan will be at a rate we set. The rate

> with respect to the amount of the loan will never be less than the guaranteed interest rate.

The policy then includes an example:

> Suppose the accumulation fund is $10,000 and there is a policy loan of $2,000. If we set the annual interest rate at 8% for amounts over $1,000 in the accumulation fund and at 6% for the amount of any loan, then interest would be credited at the rate of 4% on the first $1,000: at the rate of 6% on the next $2,000 representing the amount of the loan; and at the rate of 8% on the remaining $7,000.

Interest rates are declared on the accumulation fund based on the net returns the Company achieves on its investments. The Company achieves a net rate that is 2% less than the rate charged, reflecting the expense of processing the loan, processing loan repayments and liquidating investments to generate the amount available for the loan. This is no different from the Company's declaring an interest rate for non-loaned amounts which reflects net investment returns.

The company's practice of "retaining" or "charging" this spread of 2% on policy loans has been brought to your Department's attention in the product filing and found to be in accord with the law. Virtually all other states have comparable (if not the same) requirements with respect to loan interest rates (i.e. a "cap" of 8% on fixed rates) and none has ever found a problem with the practice.

The economic reality is that the policyholder is charged a net loan rate of 2%; the gross charge is in accord with state law, and the amount credited is in accord with the language of the insurance policy which was filed with and approved by the Department.

The Company respectfully requests that the Policy Loan Interest section of the Report be deleted as the Company's loan provisions are in compliance with Section 8 V.S.A. Sec. 3731 and have been approved by the Department.

REPLACEMENTS (Report pps. 26-27.)

Written or Printed Communications

The Report cites files containing an "Acknowledgment and Certification Regarding Sales Illustration" and/or "Computer Screen Illustration Certifications" as violations of Vermont's replacement regulation (I-88-2 § 6 A,3). As noted in the Report, this section, as it existed during the period of the examination, required the agent or broker to "leave with the applicant the original or a copy of *written* or *printed* communications used for presentation to the applicant". *(emphasis added)*. Therefore, to have such a violation would require that written or printed materials were used during the sale. However, these Certification forms evidence just the opposite - that no written or printed materials were used. Accordingly, the Company asserts that no violation of Regulation I-88-2 § 6 A,3 occurred and references to these violations should be deleted from the Report.

One of the cited files does contain a sales illustration that was provided to the applicant on the date of application. A copy of the illustration for Policy 996 604 209 UM (insured [redacted]) was attached to the Company's response of January 30, 2003 as Exhibit 7.

CONSUMER COMPLAINTS (Report pps. 28-29)

The examiners reviewed fifty complaint files and found eleven (22%) complaints to concern insureds' misunderstanding of a premium payment arrangement referred to "Accelerated Payment Arrangement" (AP). Based on that review, the Report asserts that these complaints are reasonable proof that the presentation of the AP arrangement is misleading.

The Company does not believe the facts support the examiners conclusion concerning the AP arrangement. In this instance, reliance on the percentage of AP complaint cases (22%) is misplaced. MetLife had 79 complaints from 1998-2000. During that time period the Company issued 1,155 policies. Applying the same ratio of AP complaints found the examiners, the Company would have approximately six AP complaints per year.

The cases cited by the examiners range from a 1977 issue to a 1995 issue. The Company requests the Department take note of the fact that MetLife issued almost 40,000 life insurance policies in Vermont during this period. The Company believes that this relatively small number of complaints is more appropriately viewed in the perspective of 40,000 life insurance policies issued. The small number of complaints does not provide evidence of misunderstanding about the AP arrangement.

The Company further requests the Department note that during the examination period many insurers, including MetLife, were subject to media attention and publicity that without fair evaluation encouraged policyholders to question their traditional life insurance. Although such complaints were resolved in favor of policyholders, the Company's review often found more than reasonable evidence to believe that applicants and insureds had been well-informed.

MetLife wishes to thank the Department for their consideration of the Company's comments and additional responsive materials at this time.

Exhibit 1

MetLife®

Annuity Replacement Questionnaire

Complete for Replacements Where the Proposed Contract is an Annuity (see back for Instructions)

If you are thinking about buying a new annuity contract and discontinuing or changing your existing life insurance policy or annuity contract, you should make a careful comparison of your existing benefits and the proposed benefits. Make sure you fully understand both the advantages and disadvantages of the transaction before you make a decision to replace your existing coverage.

Customer Name:____________________________ Customer Social Security Number: _____/____/______

Comparison of Existing Policy/Contract and Proposed Contract:

Existing Policy/Contract:

Company Name______________________

Contract/Account Number_______________

Issue Date_________________________

Current Account Value________________

Type of Policy/Contract:

☐ Fixed Annuity

☐ Variable Annuity ☐ Life Insurance

For Fixed Annuities Only:

Current Interest Rate ______________

Guaranteed Interest Rate ___________

Proposed Contract:

Company Name ___________________________
(if other than MetLife)

Type of Contract:

☐ Fixed Annuity

☐ Variable Annuity

For Fixed Annuities Only:

Current Interest Rate ______________

Guaranteed Interest Rate ___________

Nature of Proposed Transaction on Existing Policy/Contract:

☐ Full Surrender ☐ Partial Surrender or Withdrawal ☐ Dividend Withdrawal ☐ Loan ☐ Other _______________

Questions about the Transaction:

1. Will there be a surrender charge on your existing policy/contract as a result of this transaction? ☐ Yes ☐ No
   If "Yes", indicate the **approximate dollar amount**. $___________
2. Will you incur any tax liability as a result of the transaction? ☐ Yes ☐ No
   If "Yes", please explain.____

- For **Variable Annuity to Variable Annuity** transactions <u>only</u>. (see back for Instructions)
  Total Annual Separate Account Charges (including riders) in: Existing Contract _______% Proposed Contract _______%

Representative's Statement and Signature:

Explain why the proposed annuity contract is more advantageous for the customer than keeping the existing life insurance policy or annuity contract intact. *(Attach separate page if necessary)*

____

____

____

____

Customer's Signature:

By signing below, I acknowledge that I have read and understand the information noted above. I acknowledge that I am aware of any sales charges, including surrender charges, and tax liabilities, if any, associated with this transaction; I acknowledge that I am aware of the charges, including surrender charges, and the surrender period associated with the new annuity for which I am applying; and, I conclude that this transaction is in my best interest.

Customer____ **Date:**________________

Representative's and Manager Signature:
Completed By: **Reviewed By:**

Financial Services Representative________________________ Manager________________________

Date:________________ Date:________________

Note: This form is not a substitute for state replacement requirements and must be used in addition to those forms and duties. This form is not required in the state of New York.

AnnReplQuest (0402)

Instructions for Completing the "Annuity Replacement Questionnaire"

The "Annuity Replacement Questionnaire" must be completed whenever an annuity is purchased and, as part of the transaction, the values of an existing annuity or life insurance policy will be or are likely to be affected. This will include those situations in which a new annuity contract is funded with money taken from an existing annuity or life policy by way of full or partial surrender, loan or dividend withdrawal or when premium payments on an existing life policy are stopped or reduced to free up funds for a new annuity. In addition, the "Annuity Replacement Questionnaire" is required for both internal and external replacements.

1. The "Annuity Replacement Questionnaire" should be clearly hand-written or typed. Illegible forms may delay the processing of your new business application.

2. Fill out the form completely. If additional space is needed, attach another form and/or a separate sheet of paper.

   - If a surrender charge is incurred on the replacement of the existing contract, you must indicate the approximate dollar amount of the surrender charge. The approximate amount of the surrender charge must be obtained from the customer, the customer's contract/policy, or the existing carrier.

   - If the transaction involves a variable annuity to variable annuity replacement, the Total Separate Account Charges must be specified for both the existing and the proposed contract.

     <u>Existing contract charges</u>
     The Total Separate Account Charge for the existing contract can be obtained from the customer, the customer's annuity contract or the existing carrier. The Total Separate Account Charge includes the separate account charge, mortality & expenses risk charge, and the fees for any riders chosen. (Do not include 12b-1 fees, other management fees or fees for investment choices)

     <u>Proposed contract charges</u>
     The Total Separate Account Charge for the proposed contract can be obtained from the current prospectus or other authorized source such as the Client Brochure. The Total Separate Account Charge includes the separate account charge, mortality & expenses risk charge, and the fees for any riders chosen. (Do not include 12b-1 fees, other management fees or fees for the investment choices)

3. Make sure that you and your customer sign the form.

4. Leave the original of the form with your customer.

5. A copy of the form and any additional documentation should be attached to the new business application and given to your manager. Your manager needs to sign the form as well.

In order to complete the "Annuity Replacement Questionnaire" quickly and easily, we suggest you have the following items on hand:

- New business application and prospectus for the proposed MetLife contract.
- Information concerning the policy(ies) and/or contacts to be replaced.
- Sales illustrations for the proposed contract and for the existing policy(ies) and/or contracts, if available.
- Replacement disclosure forms, as required by state law.

This form is not a substitute for state replacement requirements and must be used in addition to those forms and duties. This form is not required in New York.